



Office of the City Auditor

Use of Other Jurisdiction's Contracts Report No. 0306

April 26, 2004

Under established ordinance, the Purchasing Division can acquire goods or services using solicitations or contracts awarded by other governmental agencies. Purchases made using this option must, however, adhere to the intent of the Procurement Code. Improvements in the control environment such as documenting sufficient policies and procedures, requiring Purchasing Agents to adhere to established rules, and implementing an internal review process would help ensure adherence.

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April 26, 2004

To the Most Honorable Mary Manross, Mayor
and Members of the Scottsdale City Council

Transmitted herewith is our report, "Use of Other Jurisdiction's Contracts," Report No. 0306. City staff was extremely cooperative while completing this audit and we would like to extend our thanks for the assistance provided.

If you need additional information or have any questions, please contact me at 480-312-7756.

Respectfully submitted,

A handwritten signature in cursive script that reads "Cheryl Lee Barcala".

Cheryl Barcala, CPA, CIA, CFE, CGFM, CISA, CISSP
City Auditor

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EXECUTIVE SUMMARY

An audit of the City's use of solicitations or contracts awarded by another governmental entity was included on the Audit Plan for 2002/2003. The work was undertaken to ensure that adequate controls are in place to guide the procurement of goods and services using this method.

City Charter requires that the Council set, by ordinance, the conditions and procedures that are to apply for the procurement of goods and services needed by the City. To this end, Chapter 2, Division 4, of the City Code sets out the "Procurement Code." One of the provisions within this Code provides the Purchasing Director with the authority to enter into contracts for the procurement of goods and services pursuant to specifications, solicitations, or contracts issued by other governmental entities. To use this process, the Purchasing Director must establish rules that provide assurance that any purchase made will conform to the purpose and spirit of the Procurement Code.

At the time we completed our work, we estimated that the Purchasing Division had approximately 90 active files that fell into this category. The types of goods or services obtained through this process included office furniture, cellular phone services, vehicles, playground equipment, bus fare boxes, hazardous waste response and disposal, translator services, floor coverings, as well as other items and services.

We found that the Purchasing Director needs to implement a stronger control environment to provide assurance that solicitations and contracts awarded by other governmental agencies are used because the arrangement is advantageous to the City and not simply to avoid the time and resources necessary to conduct an evaluation of the City's actual needs and to determine the most appropriate vendor to provide those services. We reached this conclusion because 1) the Rules, established by the Purchasing Director to guide the use of solicitations or contracts awarded by other governmental agencies, have not been followed and 2) the Policies and Procedures that govern this process are limited and provide no framework for Procurement Agents.

We also used the findings from a random sample of twenty contracts from active and inactive files to support the need for a stronger control environment. From these twenty contracts, we found several procurements made using a contract awarded by the State of Arizona even though a formal solicitation had not been conducted. According to the Purchasing Director, solicitations or contracts awarded by another governmental entity were only to be used if a formal solicitation had been conducted.

In another situation, multiple contracts for the installation of playground equipment were administratively awarded even though we believe the scope of

work met the definition of construction. City Code requires that City Council award these types of contracts. In two cases, the scope of work deviated significantly from the original solicitation conducted by the originating municipality and change orders, for additional services not included in the original solicitation, were approved by the user department and processed by Purchasing staff.

One award was for response to hazardous material spills and routine hauling and disposal of hazardous waste. These activities create a significant risk to the City. There was no documentation within the file to indicate that the Risk Management Director had approved the use of the award and no Certificates of Insurance were on file at Risk Management to indicate that the City had been named as an additional insured. The official contract file at Purchasing did not contain all of the required Certificates of Insurance.

The ability to enter into contracts for goods or services pursuant to specifications, solicitations, or contracts awarded by other governmental agencies can be advantageous to the City. For example, the State of Arizona may be able to obtain a more favorable contract for the purchase of vehicles simply because of the volume of vehicles needed on an annual basis. If the City can use this contract and purchase the vehicles for the same price offered to the State, the City achieves a direct cost savings through the reduced price of the vehicles and soft dollar savings by eliminating the need for staff to issue a bid, evaluate responses, and, ultimately, notice the successful bidder.

There may be situations in which it would not be in the best interest of the City to use a contract. For example, market conditions may have changed since the solicitation and award was completed and the City may be able to obtain a better price or newer model by conducting its own solicitation.

With well-developed, established rules, the Purchasing Division can take advantage of situations which may be advantageous and avoid using existing contracts simply because it is more expedient.

ACTION PLAN

No.	Recommendations and Management Response
	The Purchasing Director should:
1.	<p>Take steps to strengthen the control environment by:</p> <ul style="list-style-type: none"> • Developing and documenting detailed policies and procedures to provide the framework within which Purchasing staff can operate without the need for direct supervision. These procedures should be sufficient to ensure: <ul style="list-style-type: none"> ○ Compliance with provisions set out in City Code. ○ Goods and services purchased with another governmental entity's contract are the same as what was solicited. ○ Procurement Agents document factors, risks, and steps taken to mitigate the risk when determining that a solicitation or contract meets the needs of the City. ○ Periodic review of the Rules, and the accompanying Procedures, is undertaken to update the Procurement Code when needed. • Establishing and documenting clear parameters to guide situations that are considered to be exceptions. • Establishing and implementing appropriate monitoring tools when duties are delegated. • Requiring segregation of duties between the evaluation process and the award. • Establishing the content and the frequency of reports that are to be provided to management so that effective oversight can be exercised over the use of other jurisdiction's contracts.
	<p>Management Response: Agree with intent. See page 14 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: 7/31/04</p>
2.	<p>Require that Procurement Agents prepare a written justification for the use of the solicitation or contract and ensure that the documentation is retained as part of the official contract file.</p>
	<p>Management Response: Agree in part. See page 15 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: 7/31/04</p>

No.	Recommendations and Management Response
3a.	Ensure that Procurement Agents adhere to established procedures or eliminate procedures that no longer add value.
b.	Modify practices to ensure that any purchases made using a solicitation or contract awarded by another governmental entity are reported on the applicable weekly "Report of Solicitations Issued or Contracts Awarded." If not, then modify the Procedure set out in P2-191.4 to clarify the intent to only report situations that exceed the formal procurement limit.
	<p>Management Response: Agree. See page 18 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: 7/31/04</p>
4.	Develop a process that provides documentation sufficient to prove that a "Notice of Intent to Award" was posted on the day indicated on the Notice and remained posted for the required period.
	<p>Management Response: Disagree. See page 19 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: N/A</p>
5.	Require Procurement Agents to obtain positive confirmation from the requestor that consideration was given to environmental products or needs when requesting use of another governmental entity solicitation or contract. Procurement Agents should be required to note whether or not the solicitation or contract used by the other governmental entity contained language that would have restricted use of environmentally friendly products.
	<p>Management Response: Agree in part. See page 20 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: N/A</p>
6.	Ensure that the Risk Management Director, the Purchasing Director, and, if applicable, the City Attorney, review requests to use a solicitation or contract awarded by another governmental entity to determine if there is any risk that requires mitigation or other factors that should be weighed prior to making the decision. This review should be documented and, for requests that are subsequently approved, notice should be sent to the Risk Management Director for inclusion of the "contract" on the database used to track Certificates of Insurance.
	<p>Management Response: Agree with intent. See page 23 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: 7/31/04</p>

No.	Recommendations and Management Response
7.	Clarify when a Notice of Intent to Award is to be posted if the initial Purchase Order created under a solicitation or contract awarded by another governmental entity falls under the formal procurement limit but a subsequent Purchase Order exceeds the limit or the cumulative value during a specified time period reaches the formal limit.
	<p>Management Response: Agree in part. See page 26 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: 7/31/04</p>
8.	Require that Procurement Agents obtain the required Certificates of Insurance prior to issuing a Purchase Order or Notice of Award and verify, on a routine basis, that the Certificate continues to be in force prior to issuing any subsequent Purchase Order.
	<p>Management Response: Agree. See page 27 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: 7/31/04</p>
9.	Ensure that construction contracts are not administratively awarded unless the construction activity clearly falls into the category of routine maintenance.
	<p>Management Response: Disagree. See page 29 for full text of response.</p> <p>Responsible Party: Purchasing Manager/Director Completed By: N/A</p>
10.	Establish procedures to ensure that solicitations or contracts awarded by another governmental entity are not used to obtain goods or services that were not specifically solicited or included within the contract issued by the other entity.
	<p>Management Response: Disagree. See page 33 for full text of response.</p> <p>Responsible Party: Purchasing Director/Manager Completed By: N/A</p>
11.	If the practice of using solicitations or contracts awarded by "set aside" is to continue, either 1) draft and submit for Council consideration, an amendment to the City Procurement Code that gives preference to goods and services manufactured by the Arizona Industries for the Blind, Arizona Correctional Industries, and certain non-profits if the quality and the pricing is similar to what is available in the private sector or 2) develop and post for consideration, a Purchasing Rule that documents the process for "set asides."
	<p>Management Response: Disagree. See page 37 for full text of response.</p> <p>Responsible Party: Purchasing Manager Completed By: N/A</p>

BACKGROUND

The City Council is responsible for setting, by ordinance, the conditions and procedures that apply when the City needs to procure goods or services.¹ To provide this structure, multiple ordinances have been adopted over time and codified into a section of the City Code titled, "Procurement Code" (Code).

Provisions in the Code outline a centralized Purchasing Division under the supervision of a Purchasing Director (Director). The purpose of establishing the Code is to:

- Establish efficient procurement and surplus property procedures.
- Secure the City materials, services, and construction at the lowest possible cost commensurate with quality needed.
- Exercise positive financial control over purchases.
- Clearly define authority for the purchasing function.
- Assure the quality of purchases.

Under the Code, the Director is required, among other things, to procure all materials, services, and construction required by any department of the City; establish rules and procedures for the management of inventories, of material, and surplus personal property belonging to the City; and discourage uniform bidding to obtain as full and open competition as possible on all purchases.

The Code sets the threshold for formal procurements at \$20,000 with an annual limit adjustment. When purchases exceed this limit, issuance of an invitation for bid or, if the Director determines, use of competitive sealed proposals is required. For procurements less than this, purchases are made in accordance with Procedures set out by the Director.

The Code sets the authority to award contracts. Only the City Council has the authority to award contracts for professional services and City construction projects that exceed the formal limit. For all other purchases, the Director has the authority to award contracts administratively. To provide assurance that Council is aware of formal procurements awarded in this manner, a "Report of Solicitations Issued or Contracts Awarded" is provided weekly.

To provide structure for the purchasing function over and beyond what is set out in the Code, the Director has developed Rules governing the procurement of goods and services. The Code provides the authority for the development of these additional Rules as long as they are consistent with what was established by Code. Before a Rule becomes effective, it must be filed with the City Clerk.

¹ Article 8, Section 3, of the Scottsdale City Charter.

At least thirty days before the Rule is filed, it must be posted in one or more of the places customarily used by the City for posting public notices. This process provides notice to interested parties and solicits written comments.

Rules established by the Director include a wide range of directives such as:

- Requiring that written determinations be retained in the appropriate official record file and fully specify the reasons (R2-183.1).
- Defining a "specialty contractor" as an individual who provides staff assistance or instruction for City sponsored citizen participation programs (R2-184.1).
- Stating that the annual adjustment in the formal limit shall occur in increments of \$100 on July 1 of each year (R2-185.1).
- Providing the structure for purchases when the amount required is less than \$2,000; between \$2,000 and \$5,000; between \$5,000 and \$10,000; and over \$10,000 but less than the formal limit (R2-187.1).
- Outlining the process for obtaining professional services when formal procurement is not required (R2-187.2).
- Setting out the process to be followed for competitive sealed bids and competitive sealed proposals (R2-188 *et seq.*).
- Requiring the placement of a written justification in the contract file when awarding a contract using specifications, solicitations, or contracts awarded by another governmental unit (R2-191.1).
- Stating that the Director will prepare and make available standard contract language for contracts subject to the Procurement Code (R 2-199.1).

For enhanced service delivery, the Director has delegated certain customary and routine procurements such as:

- Engineering services associated with traffic and drainage projects to the Transportation General Manager or designee.
- Architectural, Engineering, and Construction Manager services for Capital Projects and Improvement Districts to the Municipal Services General Manager or designee.
- Engineering services for Water Resource Projects to the Water Resources General Manager.
- Human Services activities such as housing, domestic violence shelter services, etc. to the Community Services General Manager or designee.
- Property and liability insurance services to the Risk Management Director.

Procurement Process

Procurements are initiated by the submission of a Purchase Requisition.² A Procurement Agent³ is then responsible for ensuring that the correct procurement process, based on the anticipated cost of the goods or services needed, is followed. For purchases less than the formal limit, the following procedures are to be followed:

- Up to \$5,000, pricing is to be solicited from one or more vendors.
- Over \$5,000 and up to \$10,000, at least three vendors are to be asked to submit verbal or written quotes and the award is to be made to the lowest responsible bidder submitting a responsive quote.⁴
- Over \$10,000 but under the formal limit (with the exception of professional services), written quotes are to be obtained from three bidders through the submission of a "Request for Quotation." For professional services, the selection is to be made using an "Informal Request for Proposal" and an evaluation of all proposals received is to be completed.

When purchases exceed the formal limit, a bid or solicitation process must be followed. The procedures in place provide for notice to interested parties, submittal of sealed bids or proposals, a documented evaluation matrix, and, ultimately, a decision to award the services or reject all bids or proposals.

There are three unique circumstances in which procurements do not follow established procedures. First, the Code provides for the awarding of a contract for goods or services without competition if the Director makes a determination that there is only one source for the material or service. Second, the Director may authorize emergency procurements using as much competition as reasonably possible in the circumstances. Third, the Procurement Code authorizes purchasing materials and services pursuant to specifications, solicitations, or contracts issued by other governmental units.

Committing Funds and Authorizing the Purchase

When a decision has been reached to make a purchase, the Procurement Agent generates a Purchase Order. This document authorizes the vendor to provide the goods or services and sets up the mechanism for the vendor to be paid. The

² If the work unit has a Procurement Card and the purchase is less than \$2,000, the procurement may be initiated and completed by the work area.

³ Procurement Agent means the Purchasing Director, Purchasing Manager, Bid and Contract Coordinator, Bid and Contract Specialist, Senior Buyer, Buyers, Buyers Aide, or any member of the Purchasing staff authorized by the Purchasing Director. It also includes anyone authorized to use a City Procurement Card if the purchase is made using the Procurement Card.

⁴ When the cost associated with a professional services contractor or Specialty Contractor is less than \$10,000, the Contract Administrator may select the vendor to be used.

creation of a Purchase Order also serves to ensure that funds will be available to pay for the item because it places a "hold" on an amount of funding equal to the maximum limit identified on the Purchase Order. The "hold" eliminates the potential for an area to make a commitment to purchase an item and then spend the funds on unrelated transactions.

Purchases Using Other Jurisdiction Contracts

For situations in which procurements are made using specifications, solicitations, or contracts awarded by other governmental units, the Director has established several Rules that must be followed. These include:

- Requiring written justification for the use of a contract issued by another governmental agency to be placed in the contract file.
- Setting the following conditions when awarding a purchase:
 - The Director must determine that the contractual terms are advantageous to the City and the procurement process used by the other agency substantially meets the requirements of the City's Procurement Code.
 - The Procurement Officer of the other government agency must agree to allow the City to make the purchase.
 - A copy of the complete solicitation and other contract documents obtained from the other agency are to be retained in the Contract File.
 - A Purchase Order or Notice of Award is to be executed referencing the applicable contract of the other agency.

To supplement the Rules, Procedures require that any request to use a contract issued by another governmental entity include the reason for the request and the volume and value of the proposed purchase. The requestor is also required to submit a copy of the contract and a written offer from the contractor stating that the contractor is willing to sell to the City pursuant to the terms of the other entity's contract.

In addition, Procedures require:

- Review, by the Director, of the appropriateness of the purchase.
- Reporting, to the Council, purchases made using this method.
- Posting, when applicable, Notice of Intent to Award prior to making the actual award.

Finally, procedures preclude anyone other than the Director from making a commitment to purchase from an existing contract awarded by another governmental entity.

FINDINGS

Objective: Determine if controls are sufficient to ensure that other jurisdiction's contracts are used appropriately and in conformance with Scottsdale's Procurement Code.

Finding
1

The control environment needs to be strengthened.

CRITERIA: The control environment should be sufficient to provide assurance that procurements made by the Purchasing Division follow provisions of the Code and Rules adopted by the Purchasing Director. To provide this environment, the following management controls should be in place:

1. Policies and procedures to provide the framework within which Purchasing staff can operate without the need for intervention.
2. Clear parameters set to guide situations that are considered to be exceptions.
3. Appropriate monitoring tools when duties are delegated.
4. Separation of duties between the evaluation process and the award.
5. Quality control system to provide assurance that adopted Rules are being followed and identify situations in which additions or deletions need to be made to established Procedures.
6. Management reports of activity level, types of awards, and other indicators that could be used to monitor purchases made outside the usual and customary procurement process.

CONDITION: Sufficient management controls have not been implemented to provide assurance that purchases made using solicitations or contracts awarded by other governmental entities will adhere to established Rules and meet the spirit and intent of the City's Procurement Code.

1. Sufficient, documented policies and procedures are not available to guide Procurement Agents when making a decision on whether or not to use a contract awarded by another jurisdiction. The Purchasing Director has established some formal Rules and Procedures such as requiring a written determination to be placed in the contract file setting out the process for a request to be made, outlining the expectation for posting, and requiring some information to be retained within a contract file, but these are not sufficient. For example, there are no written procedures outlining:
 - The type of information to be retained in the formal contract file. There is no requirement to retain Certificates of Insurance, Notice of Award, Purchase Orders, evidence of posting, or other correspondence as part of the documentation.

- The process to be followed if more than one vendor, for the same type of service, has been qualified by another governmental entity.
 - The steps to be taken to determine if issues such as insurance or other contractual terms should be considered prior to making a decision to approve a request.
 - The steps to be taken to verify, and document, that appropriate contract extensions have been approved by the originating entity, accepted by the vendor, and whether or not any pricing changes became effective with the extension.
2. Parameters, to control when it would be appropriate to use a contract awarded by another jurisdiction, have either not been documented or are non-existent. For example, while we were told that requests would be denied if a formal solicitation had not been conducted and other parameters such as the age of the solicitation or the number of responses considered, there is nothing documented to indicate that Procurement Agents have received consistent instructions on the factors to consider prior to approving the use of a solicitation or contract awarded by another governmental entity. Moreover, there is no requirement for the Procurement Agent to document the factors considered when approving or denying a request.
 3. No process has been established to monitor duties delegated to Procurement Agents. The Purchasing Director has delegated a number of actions to the various Procurement Agents and the Purchasing Manager. While there may be informal discussions regarding the appropriateness of awards, there is no process that results in a periodic review of files to determine that there is sufficient evidence to warrant the decision that was made.
 4. No internal quality control system to ensure that the Rules are followed and adequate documentation is maintained. No individual has been assigned to conduct periodic reviews of contract files to provide feedback on the level of compliance or improvements that can be made.
 5. No management reports prepared on a periodic basis to provide information such as number of requests received, number of awards made using contracts awarded by other governmental agencies or other factors that could be used to monitor the activities carried out by Procurement Agents.

Rules and Procedures codified into the Purchasing Division's "Procurement Code" provided the only written guidance on what was to be followed when a request was made to use a solicitation or contract award made by another governmental entity. As a result, we had to rely on verbal instructions as to what was required (i.e., a formal solicitation, wording to indicate that the vendor agreed to extend the terms and pricing to other agencies, when formal Notice of

Award would occur, etc.) to identify the criteria that would be used for testing. While the Purchasing Director and Purchasing Manager were able to provide this information, the lack of documentation creates a situation in which it would be difficult to ensure that Procurement Agents received consistent instruction on the steps to follow. In fact, we experienced situations in which the Purchasing Director and Purchasing Manager initially differed on what the actual practice should be.

At the start of the audit, we questioned how we would be able to identify situations in which awards had been made so we could test compliance. We were told that the practice was to use a "purple folder" when a request was approved. Staff also provided a list of "active" and "inactive" files. We then went to Purchasing and made a visual inspection of files and compared the list to the folders found. We found that information within the files was inconsistent with many containing only the contract obtained from an originating entity. This created a situation in which we could not tell, based on the information within the folder, whether or not a purchase was actually approved. We also noted that there was no consistency in which information was filed within the folders. While each folder contained multiple sections in which information could be filed, we could not locate, for example, Purchase Orders in the same place within each file. And, often, similar documents were filed within the same folder in multiple locations.

We noted that the use of the purple folder was not restricted to only situations in which approval was granted for use of a solicitation or contract made by another governmental entity. We found intergovernmental agreements (IGAs), a dissimilar type of transaction, filed in the same color folder. And, we found that the lists prepared by staff to set out the population of procurements made using this method were incorrect. Duplicates were listed and there were instances in which we found folders that were not on the list, as well as contracts listed that we could not locate folders for. As a result, we cannot say with certainty that we had the entire population of approved procurements from which to draw any samples for testing.

During the audit, we found limited information about what should actually be retained in the contract file. Again, we had to rely on verbal instructions. Initially, we were told that "Notices of Intent to Award" would be placed in files if the procurement exceeded the formal limit. When looking at files, these documents were not consistently filed. When we inquired about the lack of documentation, we were told "Notices of Intent to Award" were kept in a different location. The same discussion followed when questioned about the lack of Certificates of Insurance. At the conclusion of discussions, it became apparent that we would not be able to tell, based on information within a file, the volume of purchases made, either within a fiscal year or on an inception-to-date basis, whether or not the "Notice of Intent to Award" had been posted, if a Procurement Agent verified

that appropriate insurance was provided before approving the procurement, or if other factors weighed in the decision to use a solicitation or contract awarded by another governmental entity.

The limited amount of documentation within many of the files made it impossible, without additional research, to tell whether or not a purchase was made or if the request was denied. If a purchase was approved, there was no information setting out why it was advantageous for the City to use this method instead of conducting a solicitation. If the request was denied, there was no information setting out why. As a result, someone independent of the process would not be able to reach a conclusion that the Procurement Agent had sufficient information with which to make a decision.

We found that files are maintained based on the solicitation conducted and not the vendor(s) qualified to provide the services. For example, one of the contracts selected in our sample was for the removal of hazardous waste. The State of Arizona conducted the solicitation and awarded contracts to four different vendors. The contract file set up by the City contained documentation such as contracts and pricing schedules for three of the four vendors, extension information for all four vendors, Purchase Orders for environmental services procured from a different contract, Certificates of Insurance for two of the four vendors and a couple of quotes for specific tasks. There was no order to the file (i.e., vendor one documentation filed together, vendor two documentation filed together, etc.) and nothing within the file to indicate why one vendor was used in some instances and another vendor in other situations, or to indicate that the Procurement Agent checked to see that contract extensions had been granted, insurance was up-to-date, and other issues resolved prior to issuing a Purchase Order. In this particular instance, the file contained a "contract alert" from the State Procurement Office setting out that one of the vendors had requested assignment of its contract and advising that anyone using the State contract not issue Purchase Orders to this vendor. There were, however, Purchase Orders issued by the City to this vendor subsequent to the date of the "alert" but there is nothing in the file to indicate that the Procurement Agent issuing the Purchase Order was 1) aware of the alert or 2) checked to see whether or not the issue had been resolved.

Finally, blanket Purchase Orders were issued to two vendors in July and August 2003, prior to contract extensions being approved by the originating entity. Language was inserted to the effect that "the PO is only valid through 9/30/03 unless extended." We confirmed that the Purchase Orders were still open as of January 2004, but there is no evidence that the Procurement Agent followed up after issuance of the Purchase Orders to verify that contract extensions were granted so the Purchase Order would not remain open if the vendor was no longer under contract with the originating entity.

CAUSE: Management decision.

EFFECT: Purchases may be authorized that do not meet the intent and spirit of the Procurement Code. Without sufficient controls, management may have limited knowledge regarding how duties are actually carried out. This may lead to an environment in which Rules become ineffective because there is no enforcement.

RECOMMENDATION:

Take steps to strengthen the control environment by:

- Developing and documenting detailed policies and procedures to provide the framework within which Purchasing staff can operate without the need for direct supervision. These procedures should be sufficient to ensure:
 - Compliance with provisions set out in City Code.
 - Goods and services purchased with another governmental entity's contract are the same as what was solicited.
 - Procurement Agents document factors, risks, and steps taken to mitigate the risk when determining that a solicitation or contract meets the needs of the City.
 - Periodic review of the Rules, and the accompanying Procedures, is undertaken to update the Procurement Code when needed.
- Establishing and documenting clear parameters to guide situations that are considered to be exceptions.
- Establishing and implementing appropriate monitoring tools when duties are delegated.
- Requiring segregation of duties between the evaluation process and the award.
- Establishing the content and the frequency of reports that are to be provided to management so that effective oversight can be exercised over the use of other jurisdiction's contracts.

MANAGEMENT RESPONSE: We agree with the intent of this finding to strengthen the control environment by developing clear consistent procedures to direct Purchasing staff on the use of other governmental contracts. This strengthening can be accomplished by enhancing both rules and procedures currently in Section 2-191 of the Procurement Code to be consistent with some of the City Auditor's recommended changes. We agree in the need for establishing more monitoring tools including additional reports on the use of intergovernmental contracts. Purchasing has made several changes in the documentation of the intergovernmental purchases file. A Procedural Manual has already been completed and distributed to all procurement agents. File tab dividers were ordered and received to segregate all documentation within each

file and insertion into existing and expired files has begun. The Procurement Code enhancements and changes have been identified and will be completed by July 31, 2004.

A written justification stating why it is in the City's best interest to use a solicitation or contract awarded by another governmental entity should be prepared and retained in the contract file.

Finding 2

CRITERIA: Rule 2-191.1, established by the Procurement Director, requires that a written justification be placed in the contract file when using a contract issued by another governmental entity. If this method of procurement is to be used, a determination must be reached that the contractual terms are advantageous to the City and the procurement process used by the other governmental agency substantially meets the requirements of the Procurement Code.

Section 2-183, of the City Code, requires that written determinations be retained in the official record file of the Purchasing Division.

CONDITION: According to the Purchasing Director and Purchasing Manager, a written justification is not prepared when a decision is reached to use a solicitation or contract awarded by another governmental entity.

We found no other documentation that would meet the intent of the Rule. The language used for the Notice of Award and Notice of Intent to Award is generic in nature, declaring only that the Purchasing Director has determined that the purchase arrangement is advantageous to the City. Moreover, these documents are only prepared when a purchase exceeds the formal limit. As a result, if all Purchase Orders under a specific contract fall under the formal limit, there will be no situation in which a "Notice of Intent to Award" will be prepared.

CAUSE: No quality assurance process to verify that Procurement Agents follow established Rules.

EFFECT: There is no documentation of factors considered when reaching a conclusion that the contractual terms are advantageous to the City. And, there is no discussion of the steps taken to determine that the procurement process used by the other agency substantially met the requirements of the City.

RECOMMENDATION: Require that Procurement Agents prepare a written justification for the use of the solicitation or contract and ensure that the documentation is retained as part of the official contract file.

MANAGEMENT RESPONSE: Agree in part. A written justification document has been created and will be executed by the Purchasing Director, or in his absence, the Purchasing Manager and will be retained in each contract file. We

believe the city's membership in a purchasing consortium known as "Strategic Alliance for Volume Expenditures" (SAVE), which is currently made up of 87 Arizona cities; counties, towns, and various school districts met the requirement of Section 2-191. The city's membership in SAVE was approved by City Council at the meeting of 9/20/99. Entities signing the cooperative agreement and becoming members in SAVE are giving their approval for any other member to utilize their contracts if appropriate. All SAVE members have inserted a "Cooperative Purchasing" clause in their respective solicitations notifying the bidders that other entities may utilize their contract. SAVE has its own website and monthly meetings are held to discuss new contracts coming up, possibilities for joint bidding, and problem issues another entity may be experiencing. Although the City's participation in SAVE has not been added to Section 2-191 of the Procurement Code, we feel it has served as replacement for a written determination by the Director to be placed in the contract file. Prior to a contract file being created, either the Purchasing Director or Manager reviews the subject solicitation and contract to assure contractual terms are advantageous to the city. The exception to this is informal purchases under \$20,000 made by city buyers from a State of Arizona contract. The city has a Cooperative Purchasing Agreement with the State, which was approved by the City Council at the meeting of 4/14/1986 and extended annually.

City Auditor Comment: This finding resulted from non-compliance with Rule 2.191.1, not non-compliance with City Code Section 2-191. Each purchasing decision is unique to the circumstances at that point in time. The requirement for a written justification provides the ability to document the thought process (i.e., considerations given to pricing, change in market, etc.) used to reach the decision to use a solicitation or contract awarded by another governmental entity. For this reason, we believe the requirement adds value.

Finding
3

Procedures should be followed, with appropriate documentation retained, or the requirement should be eliminated.

CRITERIA: Procedures established by the Purchasing Director require:

1. Submission of a properly completed Purchase Requisition.
2. Verification by the requestor that funds are available.
3. Buying and receiving of products or authorizing initiation of service by a Procurement Agent or a person duly authorized by the Director to initiate a purchase pursuant to duly adopted Purchasing Card Guidelines.

For situations in which solicitations or contracts issued by another governmental entity are to be used, procedures also require:

1. The reason for the request, the volume and value of the proposed purchase, a copy of the contract from the other jurisdiction, and a written offer from the contractor to sell to the City pursuant to the terms and conditions listed in the contract is to accompany a request to use a contract issued by another governmental agency.
2. The Purchasing Director is to review the appropriateness and then make the purchase according to all applicable Code sections.
3. All purchases made according to Section 2-191 are to be reported to Council on the weekly "Report of Solicitations Issued or Contracts Awarded."

CONDITION: Purchase Requisitions were not consistently retained in the contract file, consequently, we could not verify that a properly completed Purchase Requisition was submitted. There was nothing to document that the requestor verified that funds were available prior to initiating the purchase. Purchasing does not require the reason for the request or the volume and the value of the proposed purchase to be provided in writing so that the information can be retained in the file. Therefore, there would be no way to verify that the procedure is being followed. There is no evidence that the Purchasing Director reviews the appropriateness of use prior to making the commitment. Finally, current practice is to report only those purchases that exceed, based on a Purchase Order, the formal procurement limit.

CAUSE: No quality assurance process to ensure that procedures are followed.

EFFECT: Practice does not adhere to established Procedures. As a result, insufficient documentation is retained within files to allow an independent review of the reason for the request and the projected value of the proposed purchase to allow a determination to be made that the use of the solicitation or contract conformed to the spirit and intent of the Code. Without a review by the Director, this form of purchase has the appearance of a routine type of transaction instead of an exception that warrants a higher level of scrutiny. Limiting the reporting of these exceptions to situations over the formal bid limit results in an incomplete picture of the number of instances in which the City chose to use a contract of another governmental entity.

RECOMMENDATION:

- Ensure that Procurement Agents adhere to established procedures or eliminate procedures that no longer add value.
- Modify practices to ensure that any purchases made using a solicitation or contract awarded by another governmental entity are reported on the applicable weekly "Report of Solicitations Issued or Contracts Awarded." If not, then modify the Procedure set out in P2-191.4 to clarify the intent to only report situations that exceed the formal procurement limit.

MANAGEMENT RESPONSE:

- Agree. A Procedural Manual specifying all documentation required in the contract file has been developed and distributed to all procurement agents. The rules and procedures contained in Section 2-191 will be enhanced in appropriate areas and deleted in others to reflect the recommendations in this Audit Report.
- Agree. Purchasing will modify Procedure P2-191.4 to read "The Director shall report any purchase or joint solicitation permitted by this section exceeding the formal bid limit to the Council on the applicable weekly Report of Solicitations or Contracts Awarded."

Finding
4

Procedures should be implemented to provide evidence that required postings occur.

CRITERIA: Rule 2-201.1 requires a "Notice of Intent to Award" to be posted at least five days prior to award when the contract will exceed the formal limit and the award will be made administratively.

CONDITION: Procurement Agents generate the "Notice of Intent to Award" and post the document for the required time. It was the position of the Purchasing Division that, if the Notice could be presented, it should be sufficient evidence that the posting actually occurred. We found, however, that the Purchasing Division could not actually prove that the posting occurred. There is no segregation between the preparation of the Notice and the actual posting, no listing prepared on a daily basis of the Notices posted, and no evidence retained to document the date that the posting was taken down. As a result, the only evidence of posting is the document itself. This is not enough to allow a determination to be made that the document was actually posted for the required time.

CAUSE: Management decision.

EFFECT: The Purchasing Division would not be able to provide evidence that the required posting actually occurred if there were a challenge.

RECOMMENDATION: Develop a process that provides documentation sufficient to prove that a "Notice of Intent to Award" was posted on the day indicated on the Notice and remained posted for the required period.

MANAGEMENT RESPONSE: We disagree with the City Auditor's recommendation that we notate when a notice is placed on the Purchasing Posting Board and when it is taken down from the Posting Board. The cost (or burden) of any control should not outweigh the benefit to be achieved. This recommendation adds no value to the procurement process and appears to be bureaucratic by its very nature. Since July 1, 1990, when the Procurement Code was first enacted by the City Council, the only challenge the Purchasing Division has received regarding proof of posting an award has been from the City Auditor in this report. We have never received a single question from another bidder regarding this issue.

CITY AUDITOR COMMENT: This recommendation could be implemented without a significant increase in cost or additional burden. Incorporating a simple requirement to initial and date the document at time of posting and again when the document was taken down would provide 1) a means for the City to identify an original Notice over a photocopy and 2) evidence that the posting actually occurred. Both benefits, in our opinion, outweigh the cost of the few seconds that might be added to the process should this recommendation be implemented.

Documentation should be retained in the contract file to indicate that consideration was given to the City's "Environmental Procurement Policy" prior to making a decision to approve a request to use a solicitation or contract awarded by another governmental agency.

Finding 5

CRITERIA: Rule 2-205.1 requires that purchases conform to the "Environmental Procurement Policy" adopted by the City Council in December 1991. This policy requires that staff consider the availability of environmentally friendly products when making purchasing decisions and provides that the Purchasing Director can give pricing preference, if needed, to obtain these goods and services.

Because purchases made using a solicitation or contract awarded by another governmental entity are to conform to the spirit and intent of the Procurement Code, evidence should be available to indicate that staff considered whether or not the purchase fell under the requirements of the "Environmental Procurement Policy."

CONDITION: Current practice does not require a Procurement Agent to document, as part of the evaluation process, whether or not the purchase fell under the guidelines of the "Environmental Procurement Policy."

CAUSE: Management decision.

EFFECT: Documentation is insufficient to allow an independent review to conclude that staff adheres to established policy.

RECOMMENDATION: Require Procurement Agents to obtain positive confirmation from the requestor that consideration was given to environmental products or needs when requesting use of another governmental entity solicitation or contract. Procurement Agents should be required to note whether or not the solicitation or contract used by the other governmental entity contained language that would have restricted use of environmentally friendly products.

MANAGEMENT RESPONSE: We agree that city staff must be cognizant of environmental factors in all procurement decisions, however, we disagree that all procurement decisions require special environmental decisions. Purchasing staff are cognizant of environmental factors, however, cost savings, product quality, and administrative efficiencies are also considered before a final purchasing decision is made. Section 2-191 does not require the consideration of environmentally friendly products before a purchase can be made from another governmental entity's contract. R2-205.1 was added to the Procurement Code to assure Environmental Policy considerations were *explored* in city conducted solicitations. We believe the spirit and intent of the Procurement Code has been met by our evaluation of the content of another entity's contract prior to utilizing it. It is also important to note that procuring from other governmental contracts is a very small percentage of the total work conducted in the Purchasing Division.

CITY AUDITOR COMMENT: While City Ordinance, Section 2-191, does not require consideration of environmental factors, it does require the Purchasing Director to establish rules to provide assurance that purchases conform to the purpose and spirit of the Procurement Code. In September 1991, a Policy Issue Resolution (PIR) was adopted by Council to promote the purchase of environmentally responsible products and services. It has yet to be retracted or replaced. The document states that it fulfills the requirement in the Procurement Code for establishment of guidelines governing the review and approval of selected materials based on considerations of recycling, energy conservation, life cycle costing, and other environmental concerns. Therefore, we believe compliance with it would be a necessary component of conforming to the purpose and spirit of the Procurement Code. The Contract File maintained by the Purchasing Division is the most appropriate place for evidence of compliance to be placed. Documentation within this file is kept according to set retention

schedules and would then be available during the life of the arrangement and for a period of time after expiration.

If the Purchasing Division fails to seek positive confirmation from requesting departments regarding identification of environmentally friendly products, then information is not available to evaluate whether or not the use of a solicitation or award made by another governmental agency is in the best interest of the City. Moreover, the practice at the time of our audit was to not document the review of the specifications used when solicitations were conducted by another governmental entity. As a result, even if the review did take place, there is no historical record to indicate that consideration was given to the availability of environmentally responsible products.

Procedures should be sufficient to ensure that Risk Management and the City Attorney, if appropriate, approves of the use of solicitations or contracts awarded by another governmental entity.

Finding 6

CRITERIA: Procedures established by the Purchasing Director require that all contracts subject to the Procurement Code are to be reviewed and approved by the Purchasing Director, the Risk Management Director, and, if applicable, the City Attorney for the purpose of including all applicable contract clauses.

CONDITION: When a solicitation or contract awarded by another governmental entity is used to procure goods or services needed by the City, a contract between the City and the vendor is not created. As a result, there is no document (other than the contract prepared by the other entity) that can be reviewed by the Purchasing Director, the Risk Management Director, and, if applicable, the City Attorney. While both the Purchasing Director and the Purchasing Manager stated that the practice is to run requests by the Risk Management Director, documentation is not consistently retained in files to indicate whether or not concerns were raised with issues such as insurance. According to the Risk Management Director, he has no authority to overrule a decision made by the Purchasing Director to proceed with an award if he does not believe the City has been properly indemnified against any risk.

The ability to award a procurement using a contract awarded by another governmental entity without requiring the same level of approval that would be necessary under normal situations creates a potential loophole. For example, one of the contracts in our sample was for installation of playground equipment. The Purchasing Director stated that it had been difficult to conduct an internal solicitation because of the indemnification clauses desired by the Risk Management Director and City Attorney. Using a contract awarded by another municipality allowed the City to obtain the needed goods.

The ability to obtain services without a contract simply based on the award of the Purchasing Director raises the question of compliance with Charter provisions. City Charter, Article 8, addresses the use of contracts. Section 2 states specifically that the City may contract for City improvements as provided by law. Language specifically indicates:

When required, all such contracts shall be executed in writing and shall be awarded to the lowest responsible bidder after public notice and competition unless the council rejects all bids.

It also raises the question as to why the City would be willing to assume the risk associated with obtaining services outside of a legally binding contractual arrangement but would not be willing to enter into a contract that provided, while perhaps lower than optimum protection, at least better protection than what was provided without a contract.

Finally, the practice of using contracts awarded by another governmental entity creates a void in the process used to inform Risk Management of arrangements in which a vendor is required to provide Certificates of Insurance. When Risk Management is required to approve a contract, the Division has advance notice and can populate a database for use in tracking vendors that should provide insurance. When a contract is not routed for approval, there is no compensating process to provide notice. As a result, Risk Management may or may not become aware of a situation that should be monitored. For example, one of the files in our sample was for the provision of hazardous waste removal and remediation services, a service that should warrant a requirement for sufficient insurance to indemnify the City against actions of the vendor. We inquired of Risk Management and were told that Certificates had not been provided to them.

We also reviewed the contract file kept at Purchasing and found no documentation suggesting that discussions had been held with Risk Management to determine whether or not there were any issues related to insurance and indemnification.

CAUSE: The practice of procuring goods and services using contracts awarded by other governmental entities without implementing sufficient compensating controls.

EFFECT: City may be at risk if a sufficient level of insurance coverage is not obtained or if contractual terms cannot be enforced due to lack of standing. The established practice creates a loophole that can be used to avoid a control point that was put in place to ensure that proper indemnification clauses and other appropriate terms were incorporated.

Moreover, current practice does not comply with Rules and Procedures formally adopted by the Purchasing Director. According to Procedure P2-199.2, "Contract Review Process," all contracts subject to the Procurement Code shall be reviewed and approved by the Purchasing and Risk Directors and, if applicable, the City Attorney. The definition of contract within the Procurement Code is:

Contract means all types of city agreements, regardless of what they may be called, for the procurement of materials, services, or construction or the disposal of personal property.

As such, while there may not be a written contract between the City and the vendor qualified by the originating governmental entity, there is in fact an agreement between the City and the vendor to provide materials, services, or construction. If the materials, services, or construction would normally be documented in a contract and reviewed by the Risk Management Director and the City Attorney, then procedures should require the same level of review and approval if some other form of agreement is used to obtain the materials, services, or construction.

RECOMMENDATION: Ensure that the Risk Management Director, the Purchasing Director, and, if applicable, the City Attorney review requests to use a solicitation or contract awarded by another governmental entity to determine if there is any risk that requires mitigation or other factors that should be weighed prior to making the decision. This review should be documented and, for requests that are subsequently approved, notice should be sent to the Risk Management Director for inclusion of the "contract" on the database used to track Certificates of Insurance.

MANAGEMENT RESPONSE: We agree with the intent of this finding, however, we believe the current process/policy is adequate and appropriate. The largest percentage of purchases made utilizing other governmental contracts are for commodities, which require no review by Risk Management or the City Attorney. Service and installation contracts all require insurance certificates and approval by the Risk Management Division when appropriate. A written procedure will be developed to ensure Risk Management receives a copy of an entity's service contract for review prior to any purchase. However, the cost (or burden) of any control should not outweigh the benefit to be achieved. To impose a requirement of having the Risk Management Department and the City Attorney's office approve all solicitation [sic] would be bureaucratic and counter productive to an efficient organization.

There are a few points stated in the "Findings" portion of this Action that requires clarification. Under the "Criteria" section, the reference is made that all contracts subject to the Procurement Code are to be reviewed by the Purchasing Director, the Risk Management Director, and, if applicable, the City Attorney. Other

governmental contracts are not "subject" to our Procurement Code. Section 2-191 of the Code specifically states "The Director may enter into contracts for procurement of materials and services pursuant to specifications, solicitations, or contracts issued by other governmental entities. Such purchases shall be made pursuant to established rules. The rules shall assure that such purchases conform to the "purpose and spirit" of this Code." Contained within the "Condition" section of this Finding, is a statement reporting that the Risk Management Director has stated "he has no authority to overrule a decision made by the Purchasing Director to proceed with an award if he does not believe the city has been properly indemnified against any risk." The auditors misunderstood the context of this statement. According to the Risk Management Director, the intent of the statement was, "The Risk Management Director has no authority to change the indemnification and insurance provisions of another governmental entity's contract the city is considering buying under. What happens in this instance is that Purchasing and Risk confer to determine if the indemnification and insurance provisions are minimally acceptable and what is the cost benefit to the city to deviate plus or minus from standard contractual provisions." Purchasing, Risk Management, and the City Attorney's office often consult about many issues that arise during contract discussions. The contract in question was discussed and approved by both divisions. The Risk Management Director and Purchasing conducted a cost benefit analysis in which the risk of exposure was compared to the savings and all parties concurred that the cost benefit to the city was compelling enough to accept the risk by utilizing this contract. The contract in question saved the city thousands of dollars.

CITY AUDITOR COMMENT: The intent of the recommendation is to ensure that the same level of review occurs regardless of the procurement method chosen. Review of contracts by the Risk Management Director adds value by ensuring that appropriate indemnity clauses are incorporated. Allowing a process to exist that results in procurement agreements that are not reviewed (and would normally be reviewed if the City conducted the solicitation and made the contract award) creates a loophole that can be used by staff to avoid requirements that may seem onerous.

While the Purchasing Director and Risk Management Director may confer when there is a question regarding whether or not to use a solicitation or contract awarded by another entity, current practice does not result in consistent documentation of the decisions reached. Nor does it result in sufficient notice to the Risk Management Division to initiate the tracking of Certificates of Insurance. As a result, we do not believe the current process/policy is adequate.

Procedures need to be implemented to ensure that procurements, exceeding the formal limit, are properly noticed.

Finding
7

CRITERIA: Procurements that exceed the formal limit, with the exception of professional services or construction, can be administratively awarded. Prior to the award, a "Notice of Intent to Award" is to be posted for five days.

CONDITION: The Purchasing Division does not require an annual estimate of the quantity and value of goods or services to be purchased prior to creating a Purchase Order. This means that an informed decision cannot be made as to whether or not the total during a fiscal year will exceed the formal limit. As a result, a Purchase Order may be initiated for an amount below the formal limit (and not posted) with a subsequent Purchase Order(s) created for additional goods or services. There is no process in place to monitor period to date purchases to identify situations in which the total of procurements reach a point at which formal notice should be made. We were told that the practice is to post any situation in which an individual procurement would exceed the formal limit, but no consideration is given to posting situations in which more than one Purchase Order, combined, would exceed the limit.

CAUSE: Management decision to not require estimated value prior to initial purchase in order to determine whether or not total purchases during the fiscal year would warrant a formal solicitation. Additionally, it is the philosophy of the Purchasing Division that it is in the best interest of the City to "spread the wealth," so to speak, and provide multiple vendors with the opportunity to do business with the City.

EFFECT: Potential for the appearance that purchases have been split to avoid the need to post formal Notice of Intent to Award. Providing an atmosphere in which multiple vendors have the opportunity, within a fiscal year, to conduct business also adds to the workload for Procurement Agents. Using the hazardous material disposal contract as an example, over the first six months of fiscal year '03/04, the City issued seven Purchase Orders to three different vendors for a total value of \$41,948. Because each of these fell under the formal procurement limit, no posting occurred and Council was not informed of the fact that these procurements were made using a State contract. But, more importantly, if proper due diligence had occurred, staff would have been required to verify contract extensions and obtain Certificates of Insurance for each of these vendors, actions that require more time than if only one vendor had been "qualified" by the City for the removal of all hazardous waste for the upcoming fiscal year.

RECOMMENDATION: Clarify when a Notice of Intent to Award is to be posted if the initial Purchase Order created under a solicitation or contract awarded by another governmental entity falls under the formal procurement limit but a subsequent Purchase Order exceeds the limit or the cumulative value during a specified time period reaches the formal limit.

MANAGEMENT RESPONSE: Agree in part. A Procedural Manual has been developed outlining procedures to satisfy this recommendation. An on-line form has been developed for city staff to request the use of another governmental agency's contract. This form requires an estimated annual expenditure amount. All amounts in excess of the formal limit will be posted and reported to City Council. In addition, all files will contain an "Expenditure Tracking Form" which will track all purchases made on that contract within a fiscal year. The Procurement Code will be examined in conjunction with the City Attorney's office to determine any areas that might need clarification.

There are a few points in the "Findings" portion of this Action that requires clarification. We believe the statement "potential for the appearance that purchases have been split to avoid the need to post Formal Notice of Intent to Award" is incorrect. In many instances, several orders may be placed against a specific contract with months between each order and made by different buyers. This practice does not constitute splitting orders. The example referenced by the City Auditor is a State of Arizona Contract for the removal of hazardous waste. The Environmental Officer for the city stated he makes a conscious effort to spread environmental work to the three local vendors. This practice is not splitting orders but a prudent business approach to ensure vendors are available for short notice, quasi-emergency factors. Hazardous cleanups cannot wait so the city enjoys a good relationship with several vendors. This was the State's intent when making multiple awards on many of their contracts. Again we call your attention to the SAVE Intergovernmental Purchasing Group Agreement, which has been approved by City Council at the meeting of 9/20/99 and of which the State of Arizona is a member.

***CITY AUDITOR COMMENT:** We stand by the statement that the effect of the lack of established procedures creates the potential for the appearance that purchases have been split to avoid the need to post notice of award. The case referenced in the report is a prime example. In one particular instance, a Purchase Order was issued to a vendor on July 28, 2003, for \$15,000 and a second Purchase Order, to the same vendor, was issued August 5, 2003, for \$10,000. There is no documentation within the file that would allow a reasonable person to conclude that the scope of services sought with the second Purchase Order differed significantly from the first and, therefore, was not a split purchase. As a result, it has the appearance that the commitment was split to avoid the requirement for posting.*

Services performed by these vendors generally consist of routine hazardous waste removal for the Water Campus, waste oil removal at the Corporation Yard, and the hazardous household recycling program. Because these are routine services, staff in the Purchasing Division should be able to project the anticipated volume of services, using prior years experience, to determine whether or not the arrangement needs to be posted.

Procedures need to be sufficient to ensure that Certificates of Insurance are obtained.

Finding 8

CRITERIA: Certificates of Insurance, naming the City as an additional insured, should be obtained prior to the issuance of a Purchase Order for procurements made using solicitations or contracts awarded by another governmental entity. To ensure that these procurements conform to the intent and spirit of the Procurement Code, procedures should be such that the same level of documentation is obtained regardless of the method used to make the procurement. The City should be at no greater risk than what would exist if a contract would be prepared between the vendor and the City.

CONDITION: There is no documentation to indicate that Procurement Agents have been instructed to verify that appropriate insurance has been provided prior to issuing a Purchase Order. There is no requirement for Certificates of Insurance to be placed in a contract file to provide a mechanism for a Procurement Agent to easily verify that the vendor complies with requirements.

CAUSE: Lack of procedures.

EFFECT: The City obtains Certificates of Insurance in order to limit risk. If Certificates of Insurance are not obtained, the City may have little legal recourse in the event that something happens.

RECOMMENDATION: Require that Procurement Agents obtain the required Certificates of Insurance prior to issuing a Purchase Order or Notice of Award and verify, on a routine basis, that the Certificates continues to be in force prior to issuing any subsequent Purchase Order.

MANAGEMENT RESPONSE: Agree. The Procedural Manual is already developed and in place. This manual assures proper Certificates of Insurance have been obtained and placed in the file. The Rules and Procedures currently in Section 2-191 of the Procurement Code will be enhanced to reflect this recommendation.

Finding
9

Procedures should ensure compliance with provisions set out in City Code.

CRITERIA: According to City Code, Section 2-201, "Award of Contract," the City Council shall award all contracts for construction and professional services exceeding the formal procurement limit (currently \$20,000).

CONDITION: Out of twenty contracts reviewed, we found that one contract, issued by another governmental entity, had been used to procure construction services but the procurement had not been taken to Council for approval. This contract, for the removal of old playground equipment and the installation of new had been used in multiple situations. In at least four instances, the value of the purchase and installation exceeded the formal limit (\$39,647.15, \$66,575.09, \$69,350.64, and \$63,356). But, instead of taking the awards to Council, they were made administratively.

We made our determination that this contract was for construction based on language within the contract document used by the other governmental entity. The contract required temporary fencing around the entire project until final acceptance; signs on fencing with the wording "Danger, Area under Construction, Do not Enter," referenced a "pre-construction walk through," and the need to protect the public from "hazards due to construction activities." The contract also called for a performance surety bond and set out liquidated damages should the contractor fail to deliver or perform the services within the time frame specified.

We also verified that the scope of services did not fall under the classification of "routine maintenance." In three of the instances, the scope of work was for the installation of new playground equipment at an area where there had not been a previous playground. In the fourth situation, the work resulted in the complete removal of old equipment and the installation of a complete new playground design.

CAUSE: Management decision. According to the Purchasing Director, it is the view of Purchasing that playground equipment installation does not fall under the definition of "construction."

EFFECT: Current practice does not adhere to City Code. There is no language within City Code that would serve to eliminate certain types of construction activities from the requirement that Council award the contract. In fact, within the Procurement Code specifically, there is a definition of construction that supports our conclusion that these activities should have been submitted to Council for approval:

***Construction** means the process of building, altering, repairing, improving, or demolishing any public structure or building or other public improvements of any kind to any public real property. Construction does not include the routine operation, routine repair, or routine maintenance of existing structures, building, or real property.*

Moreover, the practice of allowing the City to award construction activities without requiring a formal contract between the vendor and the City precludes the City being able to require the same level of protection that was a requirement of the other municipality. In this particular instance, while the awarding municipality was able to require the vendors to provide performance bonds and provide for the payment of liquidated damages, the City has no standing with these contractual terms. In this particular instance, there is nothing in the file from either vendor agreeing to extend the contractual terms to the City.

RECOMMENDATION: Ensure that construction contracts are not administratively awarded unless the construction activity clearly falls into the category of routine maintenance.

MANAGEMENT RESPONSE: We disagree with this finding. In the opinion of the Auditor, the purchase, removal, or installation of playground equipment meets the definition of construction. The Procurement Code uses a standard definition of "construction" as the process of "building," altering, repairing, improving, or demolishing any public structure or building, or other public improvements of any kind to any public real property." Purchasing has discussed the question of contracting at great length with the City Attorney's office and we agree that the definition of construction does not include "installing" materials or equipment. This interpretation of the definition of contracting is shared by most governmental agencies. Had the city intended to include installation of equipment as part of construction activities, the Code could have been made so specific. The contract in question contains several references to the specific activity of "installation" or the use of an "installation contractor," e.g., Sections 2.2, 2.5, 2.8, 2.9, and 2.10. Within the Findings section of this action, the suggestion has been made that playground equipment installation is considered by the City Auditor to be "construction" because of the requirements for temporary fencing, signage referencing an area under construction, a reference to a "pre-construction walkthrough," a concern over public risks from "hazards due to construction activities," and requirements for a performance bond and

liquidated damages. None of these criteria, however, are exclusive to a construction contract. All of these items or requirements, fencing, signage, hazards to the public, as well as bonds and liquidated damages can just as easily be associated with repair or maintenance activities, which the City Procurement Code expressly excludes from the definition of "construction." The contract referenced in this finding was conducted and awarded by the City of Phoenix Procurement Department, not their Public Works Department and the City of Phoenix Procurement Department does not bid or award construction projects. We contacted the City of Phoenix Procurement Department and were informed the contract in question was considered a contract for the 'purchase and installation' of playground equipment and not a construction contract. The City of Chandler also utilizes this contract for the installation of playground equipment and does not consider this activity as construction. The Scottsdale City's Attorney's office does not consider this activity to be construction, and additionally, according to the City's One-Stop shop, no permit is required for this activity as it is considered equipment installation and not subject to inspection, hence it does not fall under the definition of construction. Therefore, we believe Section 2-201 of the Procurement Code has not been compromised as suggested by the City Auditor.

In addition, the City Auditor's "Effect" within this Finding states "In this particular instance, there is nothing in the file from either vendor agreeing to extend the contractual terms to the City." On the contrary, Page 7 Item 1.17 of the solicitation conducted by the City of Phoenix states, "Bidder agrees to extend all terms and conditions of his offer to other municipalities, school districts, and governmental agencies of the State and hereby agrees to supply the products/services as described in Section 2, Scope of this bid, to the applicable agencies." Unless the bidder expressly took exception to this clause in the solicitation, he is bound by this requirement.

CITY AUDITOR COMMENT: In our professional opinion, the scope of services procured under this arrangement resulted in public improvements to public real property and would, therefore, meet the definition of construction as set out in the Procurement Code.

How the City of Phoenix or the City of Chandler characterizes the scope of services is irrelevant. Each municipality has unique requirements and definitions governing the actions taken by those agencies. We also believe the argument that the services are not construction because there is no requirement for a permit is flawed. There are construction activities that can be accomplished without a requirement for a permit (construction of a fence, within the height limits, for example) and instances of installation or routine repair that do require permits (installation of a water heater, for example).

City of Phoenix, the originating entity, required the vendor to provide a performance bond as well as requiring liquidated damages if installation was not completed within the timeframe required. While the solicitation document prepared by Phoenix does state that the bidder agrees to extend all terms and conditions of his offer, there is nothing within the Contract File to indicate that the contractor agreed to extend the terms and conditions outlined in the City of Phoenix contract to the City of Scottsdale. If the language in the solicitation is sufficient to enforce extension of contractual terms (as opposed to a simple agreement to extend pricing) then why was the vendor not required to post a performance bond prior to starting the work?

Procedures should ensure that goods and services, purchased with a solicitation or contract awarded by another governmental entity, are the same as what was solicited.

Finding
10

CRITERIA: The procurement of goods and services using solicitations or contracts awarded by another governmental entity is to comply with the spirit and intent of the City Procurement Code. To comply with the spirit of the Code, goods and services purchased using this method should be the same as what was originally solicited by the other agency. Under City Code, Section 2-200, contract modifications can only occur 1) if the original contract provided a mechanism for change orders and 2) if the Purchasing Director determines that contract modifications are advantageous to the City.

While there is no actual City contract when using a contract awarded by another governmental entity, the requirements set out in other sections of the Procurement Code should still be followed.

CONDITION: In one of twenty contracts reviewed, we found one situation (two separate instances) in which the goods and services procured using this process differed significantly from the type of services solicited by the other governmental entity. The solicitation conducted by the other entity was limited to 1) purchase of playground materials, 2) labor to install the items purchased (as a percent of the cost of the equipment), and 3) miscellaneous labor (per hour) for relocation of equipment and repairs. Site excavation for new playgrounds, resilient flooring materials, and other services were specifically excluded. In fact, the originating municipality conducted a separate solicitation for the installation of resilient flooring and sand.

The City used one of the two vendors qualified by another municipality to install new playground equipment at El Dorado and McCormick Railroad Park.

- At El Dorado Park, installation of concrete curbing was included in the original Purchase Order (dated August 3, 2001). This type of service was not included within the original specification and there is no indication that the

originating municipality included this type of service after award. The amount added totaled \$7,218.60 for 454 linear feet of curbing (\$15.90 per foot).

More than seven months after the date the original Purchase Order was awarded, a modification was prepared by the Procurement Agent. This add-on for "additional labor for subsurface/sidewalk for ADA access" increased the total amount by \$5,797.50. Then, two months later another modification for \$3,353.52 was processed to increase the Purchase Order for services required to provide and install 146 linear feet of "Navajo White Fence 3 foot." In both cases, the request to modify the Purchase Order was submitted to Purchasing after the vendor had completed the work.

- At McCormick Railroad Park, the initial Purchase Order included \$11,853 in services related to the installation of 150 linear feet of concrete curbing. It appears that the significant price difference from the \$15.90 per linear foot paid the same vendor five months prior for curbing and the \$79.02 per linear foot charge for this installation is due to the additional site work needed for excavation and dirt removal. There was no detail, however, to break out the cost of the curbing, excavation, and dirt removal. Similar to the issue with El Dorado Park, none of these services were included in the original solicitation. Then, six months after the initiating Purchase Order was processed, a modification was sent through adding \$4,545.50 for "wall demo" and deleting \$4,853 for curbing.

We believe that these modifications did not fall within the scope of services to be provided by the vendor. There were no provisions in the originating contract for change orders⁵ and no indication within the contract file that the Purchasing Director approved any modification. Under City Code provisions, both of these conditions would have been required before the scope of services could have been modified.

Within the contract file, there was no documentation setting out why this particular vendor was chosen to complete the installations at these two parks. According to the Purchasing Director and Purchasing Manager, possibly the vendor was used in order to match existing equipment or because the other vendor could not meet the time frame needed. Whether or not this is the case or just speculation, cannot be confirmed because there is nothing to indicate that the Procurement Agent even asked the Contract Administrator whether or not bids had been obtained from both of the qualifying vendors in order to demonstrate that the pricing obtained from the chosen vendor was equal to or better than the bid from the other qualified vendor. And, there is nothing in the

⁵ Standard contract language allowed for changes in the specifications, methods of shipment, or packing, place of delivery, time of delivery, quantities, and price but did not provide for additional services beyond what was initially bid.

file to indicate that the other qualified vendor could not do the work or was not appropriate for consideration because of the type of equipment needed.

Finally, while the originating municipality required the vendor to certify that the vendor had the appropriate contractor's license for the installation of playground equipment, there is nothing in the Purchasing file to indicate that someone verified that the contractor had the appropriate license required for concrete work over and above what would be necessary for the playground equipment.

CAUSE: Lack of adequate procedures.

EFFECT: Non-compliance with Charter provisions that require the bidding of City improvements and award to the lowest responsive bidder. Goods and services obtained did not match what was solicited by the originating entity and there was no documentation that the City obtained quotes for the work outside the contract's scope before issuing a Purchase Order and no review of the pricing to verify that the City paid an appropriate amount for the services rendered.

RECOMMENDATION: Establish procedures to ensure that solicitations or contracts awarded by another governmental entity are not used to obtain goods or services that were not specifically solicited or included within the contract issued by the other entity.

MANAGEMENT RESPONSE: We disagree with this finding. By adopting Section 2-191 of the Scottsdale Code, the City Council determined Scottsdale may enter into contracts awarded by other governmental entities as an appropriate exercise of expending City funds. While such purchases must conform with the "purpose and spirit" of the Scottsdale Procurement Code, there is no expectation that the governmental entities' procurement process must be identical with that of Scottsdale's. Rather, the other governmental entities must only have a procurement process that "substantially meets the requirements" of Scottsdale's Code. Scottsdale's Procurement Code was, among other things, adopted to "provide increased economy in City procurement activities." By using another governmental entity's procurement process, Scottsdale is able to avoid a solicitation for each and every commodity or service it requires. The City Council, therefore, has determined it is appropriate to trust other government's procurement practices.

The Auditor's report erroneously concludes the City of Phoenix contract only allows for the purchase of playground materials, labor to install the items purchased, and miscellaneous labor for relocation of equipment and repairs. A specific examination of the contract shows it allows for site excavation and concrete placement including footings. The City of Scottsdale buyers purchased Sand and resilient flooring was purchased from another City of Phoenix contract.

The Audit Report also states "There were no provisions in the originating contract for change orders..." This statement is also incorrect. Section 28, Authorized Changes, contained in the City of Phoenix "General Bidding Instructions And Conditions of Purchase, (Service Procurements)" is the City of Phoenix's Change Order provision for this Playground Equipment Contract. This provision allows for, among other things, changes to specifications and quantities. The total curbing and fencing cost did not exceed the formal bid limit and therefore could be approved by the Director and would not have needed City Council approval. To reiterate, we disagree completely with this Finding and feel this procurement met the spirit and intent of the Code and is in compliance with the Charter provisions since the purchase and installation of Playground Equipment does not constitute construction activity.

CITY AUDITOR COMMENT: We stand by our finding that the City purchased services beyond the scope of the contract awarded by the City of Phoenix. The finding results from the procurement process used by the City of Scottsdale, not the procurement process used by the City of Phoenix.

The City of Phoenix solicited the acquisition and installation of durable play apparatus. At sites with existing playground equipment, when directed by the project manager, the vendor was to remove the old equipment, excavate the site to a minimum of six inches, and remove all old sand. When installing the play apparatus, the vendor was to excavate for footings and place concrete per manufactures guidelines.

There is no discussion within the scope of the solicitation for completion of "flat work" necessary for sidewalks, installation of permanent fencing, demolition of walls, or excavation work necessary for the construction of an entire new playground location. These were the types of services obtained by the City of Scottsdale over and beyond what the City of Phoenix had included in the initial solicitation.

The City of Phoenix solicitation included language to the extent that the City reserved the right to make changes to specifications, the method of shipment, or the quantities needed among other things. None of the changes made by the City of Scottsdale fell within these parameters. Moreover, the standard language used by the City of Phoenix stated that price increases or extensions of delivery time were not binding until evidenced in writing and approved by the Deputy Finance Director. There is no indication that the City of Phoenix agreed to add the additional services sought by the City of Scottsdale.

Regarding whether or not the total curbing and fencing exceeded the formal bid limit and could have been approved by the Purchasing Director; this argument is based on the assumption that these services could have been administratively

awarded because the amount fell below \$20,000. In order for this argument to be supported, there would need to be separate contracts or Purchase Orders for the curbing, fence installation, flat work for sidewalks, excavation and dirt removal, and the wall demolition. In each situation, separate reviews of pricing would have been required. For example, the additional labor for the sidewalk needed for ADA accessibility totaled \$5,798. If this was treated as a separate award that could have been made administratively, then at least three bids (verbal or written) would have been required and the award would have been made to the lowest responsible bidder. There is no indication that this process was followed. More to the point, the Purchasing Division did not issue the modification for the work to be done until after the work was completed (invoice from vendor dated March 27, 2002, and Purchase Order modification dated April 1, 2002).

Procedures are not sufficient to ensure that all other jurisdiction contracts used are formally solicited.

Finding
11

CRITERIA: According to the Purchasing Director, the City will not use another governmental entity's contract unless that contract was formally solicited and bid by the originating entity.

CONDITION: The City of Scottsdale used a State of Arizona contract for the purchase of picnic tables from Arizona Correctional Industries, however, that contract was not formally solicited.

The contract was not competitively bid because it was a set-aside contract. The State does set-aside contracts in preference to certain type of organizations or vendors. For example, the State buys pens from the Arizona Institute for the Blind. The same may be done for products manufactured by organizations that employ mentally disabled people. The Arizona Correctional Industries provides a wide range of items such as bike racks, bookcases, desks, picnic tables, acrylic signs, and name plates built by state prisoners. The State has a committee that reviews the pricing and the quality of the goods or services proposed for a set-aside contract. The pricing and the quality have to be comparable to what could be obtained in the open market. If so, the committee can vote to contract with the organization through the set-aside program with no competition.

A review of the solicitation documents would have disclosed to Scottsdale Purchasing personnel that this contract was not formally solicited.

CAUSE: Lack of procedures.

EFFECT: Practice does not comply with City Procurement Code, which requires that purchases made using solicitations or contracts awarded by other governmental entities to comply with the spirit and intent of the City Procurement

Code. The City's Procurement Code does not provide for the award of contracts for goods and services based on "set asides," whether it be pricing preference for minority owned businesses, women owned businesses, or preference given to purchasing goods manufactured by state prisoners.

The contract file maintained by the Purchasing Division indicated that this particular arrangement had been used to purchase picnic tables three times (March 29, 2001, for \$11,261; August 6, 2001, for \$10,113; and January 15, 2002, for \$8,075). Because each of these Purchase Orders fell below \$20,000, there was no real need to use the contract awarded by the other governmental entity. Requirements for purchases, under the formal limit, allow a procurement to be made simply by obtaining quotes from three vendors (when the amount exceeded \$10,000, the quotes would have needed to be written).

While Arizona Revised Statutes, §41-2636, provides that local public procurement units **may** [emphasis added] purchase or contract for any products, materials, and services directly from Arizona Industries for the Blind, certified nonprofit agencies for disabled individuals, and Arizona Correctional Industries without competitive bidding if the delivery and quality of the products, materials, or services meet the unit's reasonable requirements, the Purchasing Director has not documented, by formal Rule or Procedure, that this is the policy of the City. The term "may" provides a level of permissiveness and does not require the City to purchase these items.

This discussion does, however, raise the issue of preference given to materials provided by the Arizona Industries for the Blind, nonprofit agencies for disabled individuals, and the Arizona Correctional Industries. State law requires the State Purchasing Director to appoint a committee to determine if materials and services provided by these agencies satisfy the requirements of state governmental units and certain items are required to be purchased if the materials and services are of equal quality to the private sector. Should a similar requirement be added to the City's Procurement Code to require the purchasing of items from these agencies if the quality and pricing is similar to the private sector?

RECOMMENDATION: If the practice of using solicitations or contracts awarded by "set aside" is to continue, either 1) draft and submit for Council consideration, an amendment to the City Procurement Code that gives preference to goods and services manufactured by the Arizona Industries for the Blind, Arizona Correctional Industries, and certain non-profits if the quality and the pricing is similar to what is available in the private sector or 2) develop and post for consideration, a Purchasing Rule that documents the process for "set asides."

MANAGEMENT RESPONSE: Disagree. The city has an Intergovernmental/cooperative Purchasing Agreement with the State of Arizona, adopted by City Council allowing the city's participation in all State Contracts. In addition, the city has an Intergovernmental Agreement with the Strategic Alliance for Volume Expenditures Purchasing consortium (SAVE) an intergovernmental agreement also adopted by City Council. The "Effect" section of this Finding states, "Practice does not comply with City Procurement Code, which requires that purchases be made using solicitations or contracts awarded by other governmental entities to comply with the spirit and intent of the City Procurement Code. "In accordance with Section 2-181.D, of the Procurement Code, "Intergovernmental Agreements are not subject to this Code." Also State of Arizona Statute 41-2636 (section D) states, "...state governmental units and local public procurement units may purchase or contract for any products, materials, and services directly from Arizona Industries for the Blind, certified nonprofit agencies for disabled individuals and Arizona Correctional Industries without competitive bidding if the delivery and quality of the products, materials, or services meet the unit's reasonable requirements." The State conducts a rigorous committee review process evaluating pricing and the quality of goods and services provided by these organizations prior to awarding a contract to any of them. We believe the process followed by the State equates to a competitive process and therefore any purchase made from Arizona Correctional Industries met the spirit and intent of the Code.

CITY AUDITOR COMMENT: This finding results from non-compliance with rules set by the Purchasing Director, not whether or not the purpose and spirit of the Procurement Code was met. During the completion of this audit, we were told (by the Purchasing Director) that solicitations and contracts awarded by another governmental entity would only be used if a formal solicitation had been conducted. A formal procurement process did not take place when the State awarded the contract discussed in this finding.

It should be noted that there is no evidence of Council approval of the State Cooperative Purchasing Agreement subsequent to 1986. As this agreement is only good for a period of five years, the renewal authorized by Council in 1986 would have expired in 1991. A representative of the Purchasing Division signed the 1999 agreement, in effect through 2004. Regardless of whether or not there was appropriate authorization to enter into this agreement, it simply allows for the purchase of materials and services at prices and terms contained in the contracts between the State and those vendors.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of this audit was to determine whether controls are sufficient to ensure that other jurisdiction's contracts are used appropriately and in conformance with Scottsdale's Procurement Code.

The scope of the work was limited to compliance with the City's Procurement Code and the Rules and Procedures set forth by the Purchasing Director.

To complete the work, we reviewed the City Procurement Code, the City Charter; interviewed the Purchasing Director, Purchasing Manager, and Risk Management Director; and reviewed various documents in the other jurisdiction contract files at Purchasing. We verified posting of Notice of Intent to Award and Reporting to Council. In addition, we selected a sample of other jurisdiction contracts used by the City and examined the solicitation package and associated contract files at the State of Arizona, Arizona Department of Transportation, Maricopa County, and the cities of Chandler, Phoenix, and Tempe.

Audit work was conducted in accordance with generally accepted government auditing standards as they relate to expanded scope auditing in a local government environment and as required by Article III, Scottsdale Revised Code, Section 2-117, *et seq.* Audit testing took place between December 2003 and January 2004 with Ramon Ramirez, Stella Fusaro, and Eric Spivak conducting the work.

APPENDIX A: MANAGEMENT RESPONSE

Management chose not to submit a formal Management Letter. Complete responses can be found on the pages indicated in the Action Plan.